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#### CHAPTER IV. PROBLEMS POSED BY FFB-FINANCED CBO SALES AND DIRECT LOANS TO GUARANTEED BORROWERS

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The understatement of total direct lending in the unified budget that results from FFB financing of CBO sales and direct loans to guaranteed borrowers contributes to two problems involving the unified budget deficit:

- o That deficit inadequately measures the amount of direct federal activity that must be financed by government borrowing. To calculate a more precise measure, it is necessary to add the unified budget deficit and the off-budget deficit. 1/
- o Resources may be overallocated to activities that can be financed off-budget because of their apparent, though not real, costlessness, as measured by the unified budget.

The understatement of total direct lending and, thus, of the unified budget deficit stems from the budgetary treatment accorded sales of CBOs and direct loans by the FFB to guaranteed borrowers. As the analysis of this chapter shows, the existence of the FFB may also contribute to the misallocation of resources. By providing a source of unlimited credit, at just above Treasury interest rates, the bank has enabled the rapid growth of activities using its financing, and, in the absence of Congressional control, has made such growth a matter of executive discretion.

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1/ The off-budget deficit is the total of outlays by the six off-budget entities: the FFB, the Rural Electrification and Telephone Revolving Fund of REA, the Rural Telephone Bank (also of REA), the Postal Service, the Regional Rail Reorganization Program of the U.S. Railway Association, and the Synthetic Fuels Corporation. In recent years, the FFB, whose outlays result from CBO sales and direct loans to guaranteed borrowers, has constituted 90 percent or more of total off-budget outlays.

### UNDERSTATING THE UNIFIED BUDGET DEFICIT

As discussed in Chapter III, the net effect of the budgetary treatment of CBO sales, whether financed by the FFB or not, and of FFB direct loans to guaranteed borrowers is to transfer off-budget the outlays for some direct loans initiated by on-budget agencies. Consequently, outlay totals at agency, program, and unified budget levels are understated.

The result is that these transactions distort the interpretation of the unified budget deficit as an indicator of the amount of federal activity that must be financed by borrowing. In fiscal year 1981, for instance, the FFB's purchases of \$11.5 billion of CBOs and its direct loans of \$9.4 billion to guaranteed borrowers caused total outlays and the deficit to be understated by nearly \$21 billion (see Table 4). The reported 1981 deficit of \$57.9 billion was in fact 26.6 percent below the level of a combined unified budget deficit and FFB deficit. Between the FFB's inception in 1974 and the end of fiscal year 1981, CBO sales and direct loans to guaranteed borrowers financed through the FFB caused the actual deficit of the federal government to be understated by \$82.3 billion.

Anyone wishing to gauge the extent of the federal government's borrowing in the credit markets to finance the deficit must consider both the on- and off-budget (mostly FFB) deficits. The unified budget deficit alone is no longer an accurate measure. Nor are the unified budget deficit combined with trust funds surpluses sufficient to explain the need for increases in the debt subject to limit. <sup>2/</sup> Even if the Congress were to balance the budget, the ceiling on the debt would have to be raised to accommodate the off-budget deficit, of which FFB-financed activity is 90 percent or more each year. In fact, of the more than \$500 billion increase in the debt subject to limit between fiscal years 1974 and 1981, the FFB accounted for about 15 percent. About one in every six dollars of net new debt issued in the last seven years was for FFB activity. Thus, the utility of the unified budget deficit as an indicator of the federal government's budgetary policy has been reduced.

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<sup>2/</sup> Some of the trust funds included in the unified budget receive more funds during a fiscal year than they pay out. These trust fund surpluses are invested in Treasury securities. Thus, the increase in the debt subject to limit each year is equal to the deficit plus the debt financed by the trust fund surpluses plus any off-budget deficit.

TABLE 4. UNDERSTATEMENT OF THE UNIFIED BUDGET DEFICIT BY FFB FINANCING OF DIRECT LOANS, FISCAL YEARS 1974-1981, (In billions of dollars)

Fiscal Year	Reported Unified Budget Deficit	Amount by Which Budget Deficit Was Understated Because of FFB-Financed:		
		Loan Asset Sales	Direct Loans to Guaranteed Borrowers	Total FFB Credit Activity
1974	4.7	<u>a/</u>	0.1	0.1
1975	45.2	5.1	1.0	6.1
1976	66.4	4.1	1.9	6.0
TQ <u>b/</u>	13.0	2.1	0.5	2.6
1977	44.9	5.1	3.0	8.1
1978	48.8	6.8	3.9	10.7
1979	27.7	9.4	3.9	13.3
1980	59.6	9.4	6.8	14.4
1981	<u>57.9</u>	<u>11.5</u>	<u>9.4</u>	<u>21.0</u>
Total	368.2	51.7	30.5	82.3

SOURCES: Budget of the United States Government, Fiscal Years 1976-1982, Special Analyses on Credit; and Department of the Treasury, Federal Financing Bank News, September 1981 Report (October 26, 1981).

NOTE: Details may not add to totals because of rounding.

a/ \$50 million or less.

b/ Transition Quarter.

## POSSIBLE MISALLOCATION OF RESOURCES

FFB-financed CBO sales and direct loans to guaranteed borrowers distort the setting of priorities among programs competing for limited budgetary resources because they permit agencies to undertake activities that are never charged to them, and that never show up in the agencies' budget totals. For instance, in fiscal year 1980 the Farmers Home Administration reported outlays of \$3.0 billion. Not included in that figure, however, was a net increase of \$6.9 billion in loans financed through CBO sales to the FFB. If these outlays had been charged to FmHA, its outlays would have tripled. Similarly, REA caused the FFB to make direct loans of \$2.5 billion in 1980 by guaranteeing notes issued by rural electric cooperatives. During the same year, the Defense Department issued guarantees for \$1.9 billion of FFB direct loans to foreign countries for the purchase of military equipment. Not one cent of these loans was charged to these agencies' budgets during 1980. Thus, an agency that can use FFB financing mechanisms can present budget totals that appear smaller than other programs unable to take advantage of these techniques. This offers a significant advantage in the competition for resources over both other loan programs that do not sell loan assets and all direct spending programs--particularly during an era of budget-cutting.

## SOURCE OF THE PROBLEMS

To what extent are the problems of understating the budget deficit and the possible misallocation of resources caused by the budgetary treatment of CBO sales and of FFB direct loans to guaranteed borrowers, and to what extent do they result from the existence of the FFB itself?

### Budgetary Treatment: Root of the Problem

The budgetary treatment of CBO sales and direct loans to guaranteed borrowers is ultimately at the root of these two problems. The provisions of law that permit FmHA and REA to treat CBO sales as loan asset sales, rather than as borrowing by the agencies, allow these two agencies to lower their outlay totals, thus understating total budget outlays as well. <sup>3/</sup> Prior

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<sup>3/</sup> Because the RETRF (REA's financial operating arm) is off-budget, even if CBO sales were treated as borrowing, the

to the FFB's establishment, sales of CBOs caused outlays to be understated and resource allocation to be skewed. Thus, even if the FFB were abolished, they would continue to cause these problems.

The understatement of total budget outlays that results from FFB direct loans to guaranteed borrowers is also a matter of budgetary treatment. It results from the combination of the off-budget status of the FFB and the nonbudgetary status of loan guarantees. It can be argued that this problem is really the result of the FFB's existence and that it would disappear if the FFB were abolished or put on-budget. If the FFB were put on-budget, the outlays for FFB direct loans to guaranteed borrowers would at least be included in the unified budget totals; they would not, however, be charged to the agencies that made the guarantees.

More fundamentally, however, the problem existed before the FFB was established. In the absence of the FFB, agency guarantees of securities sold in the government securities market would still cause the level of direct lending by the federal government to be understated. This would occur because the characteristics of such securities are practically identical to those of a direct loan by a federal agency to the insurer of the securities, financed by agency borrowing. The source of funds is the same: the securities market. The borrower is the same: the security issuer. The security received by the purchaser is risk-free in both cases: a fully guaranteed instrument versus a Treasury bill, note, or bond. And the assessment of risk and of the borrower's ability to repay devolves on the agency in both instances: either as the guarantor or as the lender.

The budgetary treatment of a fully guaranteed security and a direct loan financed by borrowing, however, are quite different. A direct loan by the guarantor agency is recorded as an outlay, increasing both the agency and the unified budget outlay totals.

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deficit would continue to be understated. The off-budget status of the RETRF and of the other off-budget entities is contrary to the recommendations of the 1967 President's Commission on Budget Concepts. All the off-budget agencies should be returned to the unified budget to be consistent with accepted budgetary principles.

The borrowing by the agency is considered a means of financing and does not offset those outlays. Under the current budgetary treatment of a fully guaranteed security, however, the agency extending the guarantee does not record an outlay and the unified budget outlay totals remain unchanged.

Thus, the budgetary treatment of a direct loan financed by agency borrowing and of a fully guaranteed security sold in the government securities market is inconsistent. Although the practical effects are the same, the effects on the unified budget are not. Moreover, this inconsistency does not result from the violation of a budgetary principle, as in the case of FmHA and REA CBO sales; instead, it arises from the consistent application of budgetary concepts. The inconsistent budgetary treatment of these two financing methods does, however, illustrate the inadequacy of the existing concepts to deal with the variations of federal credit activities.

#### The FFB: Source of Unlimited Capital

Both the understatement of direct lending levels by CBO sales and fully guaranteed securities and the potential for misallocation of resources resulting from the apparent costlessness of these financing mechanisms occurred before the FFB was established. It can be argued, however, that the existence of the FFB, and the access it provides to an unlimited source of credit at near-Treasury interest rates, has facilitated the rapid rates of growth experienced since 1974 by programs using these financing techniques, and has played a role in the possible misallocation of resources. 4/

Indeed, in this period of budgetary constraints, the access afforded some agencies to abundant credit at near-Treasury rates through the FFB may have caused an overallocation of resources

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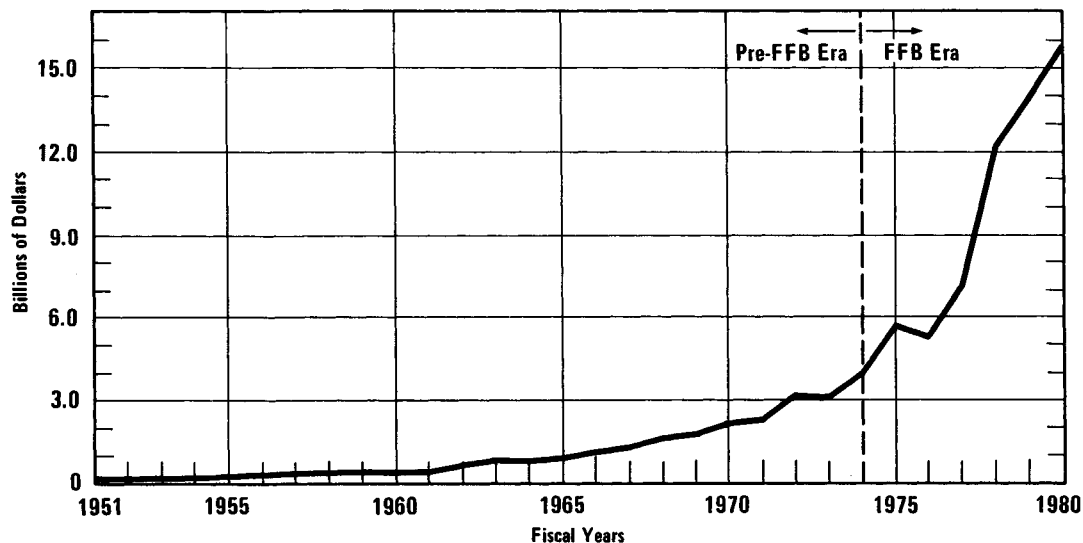
4/ As noted in Chapter II, by virtue of obtaining all its funds through borrowing from the Treasury, the FFB has effectively no limits on its activity levels during any year. Even in tight monetary conditions, the Treasury will always be able to borrow as much money as it needs. During such periods, interest rates on Treasury borrowing will rise, but compared to other rates, Treasury rates will still be less expensive. Thus, the FFB, through the Treasury, will always be able to obtain funds at good rates.

to those activities, compared to the levels of resources they would likely have received had they been forced to compete directly with all other programs. While this cannot be proved conclusively, the following examples suggest that the possibility of overallocation of resources should be considered seriously.

Farmers Home Administration Lending. The Farmers Home Administration lends directly, through three revolving funds, to farmers, small businesses, and rural communities for a wide variety of purposes. Figure 2 illustrates the levels of gross new lending in fiscal years 1951 to 1980. The level of new loans started to increase rapidly in the late 1960s and early 1970s, the period when sales of loan assets were first used extensively. New lending levels, however, exploded between fiscal years 1975 and 1980 (with the exception of 1976), right after the FFB's establishment. Between 1974 and 1980 new lending levels more than quadrupled.

Figure 2.

**New Direct Loans by the Farmers Home Administration,  
Fiscal Years 1951-1980 (End of year)**



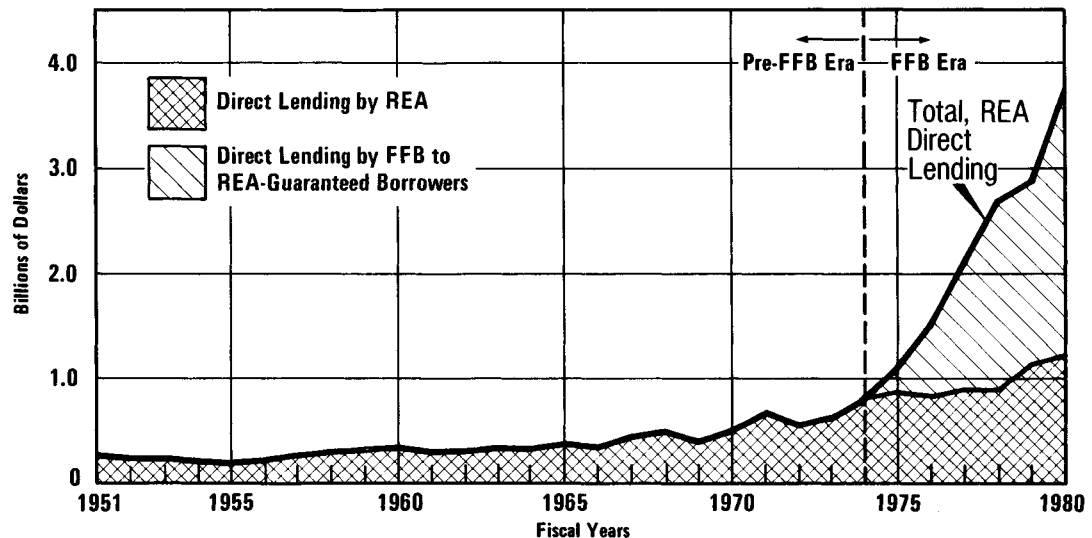
SOURCE: *Budget of the United States Government*, Fiscal Years 1952-1982, Special Analyses on Credit.

Rural Electrification Administration Lending. An even more dramatic illustration is provided by the growth in REA direct loans. As shown in Figure 3, between fiscal years 1951 and 1974,

new direct loan levels increased from about \$250 million annually to about \$850 million annually. Six years later, at the end of fiscal year 1980, new REA loans, counting both direct loans by REA and direct loans by the FFB to REA-guaranteed borrowers, totalled \$3.7 billion. Most of the growth of the FFB era occurred in the new program of FFB direct loans to guaranteed borrowers. In six years, this program went from zero to \$2.5 billion in new loans annually.

Figure 3.

### New Direct Lending by the Rural Electrification Administration, Fiscal Years 1951-1980 (End of year)



SOURCE: *Budget of the United States Government*, Fiscal Years 1952-1982, Special Analyses on Credit.

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## CHAPTER V. SOLVING THE PROBLEMS

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As awareness of the problems posed by FFB financing of CBOs and guaranteed loans has increased in recent years, various proposals have been advanced to address these problems, including:

- o Changing the FFB;
- o Improving the budgetary treatment of certain federal credit activities; and
- o Restructuring the unified and credit budgets.

Of those proposals that focus on the FFB itself, one alternative would be simply to abolish the FFB. A second alternative would be to include the FFB in the unified budget and put limits on its annual activities. Other proposals address the underlying issue--the budgetary treatment of certain credit activities that is at the root of the problems. For example, the evolving credit budget could be expanded to include limits on the volume of such transactions between various agencies and the FFB. Or, more fundamentally, the budgetary treatment of the credit transactions between agencies and the FFB could be changed to reflect their true nature, namely, as borrowing by the agencies from the FFB. Finally, one proposal would be to address the problems of budgetary treatment of CBOs and fully guaranteed loans as part of a general restructuring of the unified budget, one aspect of which would be to separate all forms of credit activity into a distinct credit budget.

Each of these proposals addresses different aspects of the problems posed by the FFB financing of federal credit activities. The following questions should be asked about each alternative:

- o Does the alternative improve the utility of the budget deficit as an indicator of federal borrowing requirements?
- o Does the alternative improve the allocation of resources through the budget process?

- o Does the alternative ensure that the financing of all obligations backed by the full faith and credit of the United States government is accomplished efficiently and at the lowest possible interest rates?

Ideally, any proposal to solve the problems posed by FFB transactions would satisfy all three criteria: it would eliminate the understatement of the budget deficit; it would improve the budgetary treatment and control of credit activities, thus improving the allocation of resources; and it would facilitate the financing of all full faith and credit debt at the lowest possible interest rates. The current budgetary treatment of the FFB and its transactions satisfies only the last of these. The following sections describe the alternatives and evaluate them according to these criteria.

#### CHANGING THE FFB ITSELF

Two proposals would change the FFB itself. The first would simply abolish the FFB, while the second would put the FFB on budget and limit its activity levels. Neither proposal addresses the underlying issue: the budgetary treatment of CBOs and of FFB direct loans to guaranteed borrowers.

#### Abolishing the FFB

Removing the FFB as a source of off-budget financing for loans and loan guarantees could be accomplished by simply abolishing the bank. As a result, agencies attempting to sell loan assets and borrowers with guarantee commitments from federal agencies would be forced to turn to the private credit market and pay higher-than-Treasury rates of interest. In addition, agencies selling their own debt, under borrowing authority, would have to sell it in the market. Thus, this alternative would effectively return federal credit activities to the pre-1974 situation, before the bank's establishment.

By returning to the pre-1974 conditions, the gains in efficient financing that were achieved through the FFB, particularly those for the financing of agency debt, would be lost. This advantage could be retained by including in the legislation to abolish the FFB provisions requiring agencies with borrowing authority to sell their debt to the Treasury Department. Forcing

loan asset sales and fully guaranteed securities back into the private securities market, however, would result in higher interest rates on these obligations, because of the degradation of the market's efficiency by the entry of a large number of relatively small offerings.

Abolishing the FFB might reduce, in part, the understatement of the budget deficit that occurs through FFB financing of credit instruments outside of the unified budget. It would also eliminate the access to an unlimited source of cheap credit for qualifying agencies, and thus, the potential for overallocation of resources to these programs. Because this option would not change the underlying budgetary treatment of CBO sales and FFB direct loans to guaranteed borrowers, it would not, however, eliminate the basic problems. In particular, this solution would do nothing to reduce the impact of federal credit activities in the market.

#### Putting FFB On-Budget

A second proposal that addresses the FFB directly would put the FFB on-budget. Legislative proposals to amend the FFB's charter to that effect have been introduced in recent years. The most recent version, H.R. 2566, the Federal Financing Bank Act Amendments of 1981, would:

- o Include the receipts and disbursements of the FFB in the unified budget; 1/
- o Limit the extent to which the FFB could purchase obligations during any fiscal year to amounts approved in advance in appropriation acts; and

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1/ Treasury officials, testifying on H.R. 2566 and its predecessor legislation, have argued that the language mandating inclusion of the bank's receipts and disbursements in the budget would require counting as outlays FFB's purchases of agency debt, which are now treated as intragovernmental transactions between agencies. This would cause double counting--once when the money is borrowed by the agency and again when it is spent. The Treasury officials suggest merely repealing the existing statutory language excluding the bank's receipts and disbursements from the budget, and then allowing normal accounting rules to determine the bank's budget authority and outlays.

- o Provide that a guarantee by a federal agency of any obligation ordinarily bought and sold in the investment securities markets should not be effective unless the obligation is held by the FFB or the guaranteeing agency.

The first provision, repeal of the FFB's statutory exclusion from the unified budget, would cause the budget authority and outlays for loan asset purchases and direct loans to guaranteed borrowers to be included in the unified budget totals. The result would be to increase the deficit. The fiscal year 1980 deficit would have increased from \$59.6 billion to \$73.9 billion under these conditions. The deficit for 1981 would have increased from \$57.9 billion to \$78.9 billion and the 1982 deficit is estimated to increase by \$16.6 billion. 2/

The second provision requires the Congress to set a ceiling on total FFB purchases for a fiscal year. Simply setting a ceiling on total FFB activities, however, would not significantly improve the ability of the Congress to allocate resources efficiently. Even if the FFB was placed on-budget as a separate entity, the initiating agencies would still not be charged with the budget authority and outlays for their FFB-financed lending. In the absence of any Congressional decisions on which of the FFB's clients should receive financing, and how much they should receive, Treasury officials would be forced either to ration credit administratively among competing claimants, or simply to allow the allocation to be determined by a "race" among the competing clients to get to the "FFB window" before all funds were exhausted for a fiscal year. Neither alternative would result in a satisfactory allocation of FFB financing.

If agencies requested more loan financing than the FFB's ceiling would allow, those agencies not able to obtain FFB-financing for direct loans might then turn to the securities market. This raises the possibility that guaranteed loan assets or fully guaranteed securities sold to investors would bear interest at rates exceeding the Treasury's borrowing rates, thus

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2/ This is the OMB July Mid-Session Review estimate for 1982 FFB outlays. Putting the FFB on-budget would increase the deficit by that amount if one assumes that there would be no change in the amounts of FFB financing desired by its client agencies. It is possible that the amount of FFB financing requested would decline if that financing were recorded in the budget totals.

sacrificing the gains in financing efficiency that the FFB was established to provide. It would also mean that those agencies could continue to finance their activities outside the budget, meaning that the budget deficit would again be understated and the possible misallocation of resources would occur.

The third provision of H.R. 2566--rendering guarantees of obligations sold in the investment securities market invalid unless the obligation was held by the FFB or a federal agency--is an attempt to address this problem by closing the door to market financing for 100 percent guaranteed securities and CBO sales. If this limitation could be effected, then the integrity of the budget process and the efficiency of financing might be preserved. 3/

#### CHANGING THE BUDGETARY TREATMENT OF CREDIT TRANSACTIONS

Both of the preceding proposals would make only marginal improvements over the existing situation because they, in effect, would treat the symptom of the problem--the FFB--instead of the problem itself: the budgetary treatment of the underlying transactions. A second pair of proposals would focus on the transactions themselves. The first, which would use the newly established credit budget, would set annual limits on the volume of CBOs sold to the FFB and direct loans to guaranteed borrowers made by the FFB without affecting their budgetary treatment. The second would change their budgetary treatment from that for lending transactions to that governing agency borrowing.

#### Controlling FFB Activities Through the Credit Budget

Incorporating FFB-financed activities into the unified budget totals would be politically painful: the deficit could increase by as much as \$14 to \$20 billion if the impact was absorbed in a single fiscal year. It might be desirable to phase in the incorporation of these activities into the unified budget, either by setting a future date for its occurrence, or by incorporating one

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3/ Treasury officials have expressed concerns about how it would be determined which obligations are of the type normally sold in the securities market and, thus, which would be required to be held by an agency or the FFB to continue the guarantee's effectiveness.

kind of activity in the budget one year, loan asset sales for instance, and then picking up FFB direct loans to guaranteed borrowers the next year. In any case, the Congress might wish to begin controlling the annual level of agency transactions with the FFB prior to, or instead of, incorporating them in the unified budget. This could be done, as part of the Congressional credit budget, by adding additional language to the limitations on gross new direct loan obligations or gross new loan commitments included in the appropriations for credit programs. <sup>4/</sup> The new limitations language would set ceilings not only on the amounts of new loans or new guarantees that could be extended to the public, but also on the portion of those loans or guarantees that could be financed by the FFB.

This alternative would enhance Congressional control of annual credit activity and efficient resource allocation by placing limitations on the agencies, not the FFB. The improvement in allocative efficiency would not be as complete as it could be, however, since the budget authority and outlays would still be off-budget. If the Congress devoted more attention to the effects of credit programs on outlays rather than to the levels of limitations on gross activity and on the portion of that activity financed through the FFB, agencies utilizing CBO sales and direct loans by the FFB to guaranteed borrowers could still enjoy an advantage in the competition for resources. This alternative would also maintain efficiency of financing, except if an agency could exceed the limitation on its FFB financing by going to the market to sell any loan assets or to finance guaranteed securities issued by nonfederal borrowers.

#### Changing the Budgetary Treatment of Loan Asset Sales and Direct Loans to Guaranteed Borrowers

As noted in Chapter III, it is misleading to consider the sale of a CBO as a sale of a loan asset for three reasons: (1) the agency does not transfer title to the loan or loans when they are sold; (2) the agency continues to service the loan or loans; and (3) the agency fully guarantees the repayment of principal and interest on the loans sold. In effect, the agency is borrowing by

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<sup>4/</sup> In a sense, the appropriation limitations on new lending and guarantees set on individual programs under the credit budget already set an upper bound on the amount of loans or guarantees that may be financed through the FFB.

issuing a security that is backed by the full faith and credit of the government, and that, only incidentally, represents the pool of loans. If the Congress required the sale of a CBO to be recorded as borrowing, the funds from the sales would not be treated as offsetting receipts; therefore, by selling a CBO an agency would not be able to reduce its outlays. In other words, agencies could not transfer on-budget loans to off-budget status. Agencies could sell as many CBOs to the FFB as they wished; however, the new loans represented by the CBOs would continue to be recorded as outlays in agency budgets.

The Congress could also choose to change the budgetary treatment of FFB direct loans to guaranteed borrowers. These could be redefined as direct loans by the guarantor agency and borrowing by the agency from the FFB. Instead of the agency recording a loan guarantee and the FFB recording budget authority and outlays, this alternative would record the budget authority and outlays in the agency's budget, and treat the agency-FFB transaction as borrowing, which would not affect the agency's budget totals. This treatment would accurately depict the transaction for what it is: a direct loan initiated by a federal agency.

Making these changes in the budgetary treatment of agency transactions with the FFB would satisfy all three criteria discussed on pages 33 and 34. The effect on the budget deficit would be identical to the proposal of simply putting the FFB on-budget: it would increase the budget deficit by the amount of FFB's financing of CBO sales and direct loans to guaranteed borrowers, which could be as much as \$14 to \$20 billion in any year. By recording FFB-financed lending in agency budgets, the allocation of resources through the budget process would be improved. <sup>5/</sup> The efficiency of financing would not be affected, unless agencies turned to the securities markets to finance 100 percent guaranteed securities. This loophole could be closed by prohibiting any agency from extending 100 percent guarantees for obligations to be sold in the securities market, or by rendering invalid any guarantee of an obligation of the type ordinarily sold in the securities market, as does H.R. 2566. <sup>6/</sup>

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<sup>5/</sup> The budget submitted by the President in January each year already attributes FFB outlays by agency and function on an information basis. These outlays still are not recorded in the agency, function, or unified budget totals, however.

<sup>6/</sup> If this change in the budgetary treatment of FFB direct loans to guaranteed borrowers was implemented, it is possible that

## RESTRUCTURING THE UNIFIED AND CREDIT BUDGETS

All the alternatives discussed above would make changes in the FFB or in the treatment of budgetary transactions within the existing framework of the unified budget. An entirely different approach would be to address the issues raised by the FFB and the budgetary treatment of federal credit activities as part of a general restructuring of the unified and credit budgets.

Some advocates of direct loan programs have argued that the current budgetary treatment of direct lending is inappropriate. They contend that there is a difference between an expenditure, on which there is no return to the government once the funds are disbursed, and a direct loan, on which the government can expect to receive repayments and interest in the future. <sup>7/</sup> Yet current practice treats the extension of a loan as an outlay in the year in which the funds are disbursed and the repayments in future years as negative outlays. Thus, the adherents of some direct loan programs have suggested that direct loans, which are an exchange of assets, should be removed from the unified budget and not treated in the same way as direct expenditures. Viewed over its entire term, a loan may not cost the government anything--repayments of principal and interest may exceed the government's cost of lending the funds. But recording the principal extended in the first year gives the appearance of a high "cost," proponents of this approach argue. A desire to avoid these high first-year budgetary "costs" may well have impelled lending program managers and their constituents to develop CBO sales or to push for off-budget status as a way of lowering their budget visibility. <sup>8/</sup>

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there would be an increase in the volume of partial loan guarantees--those covering less than 100 percent of the principal--as agencies tried to avoid the outlay effect of the reclassified FFB loans. This pressure for additional partially guaranteed loans could be addressed through the credit budget.

<sup>7/</sup> The counter to this argument is that not all direct spending activities are alike in their effects or operations, yet they are treated the same way. Advocates of the current budgetary treatment of direct spending programs note that all federal activities should be treated consistently in the budget, even if they are different in nature or purpose.

<sup>8/</sup> For instance, in a report accompanying the Export Expansion Act of 1971, H. Report 92-303, 92:1 (1971), p. 4, a bill to put the

Recognizing the near impossibility of controlling new extensions of direct loans and loan guarantees through the unified budget, which includes direct loans only on a net basis and loan guarantees not at all, the Congress has experimented with a credit budget in fiscal years 1980 and 1981. Through the credit budget, the Congress can set aggregate targets and ceilings on gross commitments for new direct loans and new loan guarantees, as well as limitations on the gross activity of individual programs through the appropriation process. Whether or not a direct loan is financed by the FFB is irrelevant in the credit budget, because the controls are on gross new loan and loan guarantee commitments by agency. The FFB financing of CBO sales and direct loans to guaranteed borrowers is important only as a means of lowering or eliminating a program's outlay effect on the unified budget. By removing direct loans from the unified budget, FFB financing would no longer pose a problem.

Excluding net lending from the unified budget could enhance the status of a credit budget. It would give the Congress two deficits to work with: the unified budget deficit and a credit budget deficit, which would be made up of net direct lending and net loan guarantees extended. <sup>9/</sup> To determine the total amount of federal activity to be financed in the credit markets, the Congress

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Export-Import Bank off-budget, the House Banking Committee noted:

Since the adoption of the unified budget concept, however, borrowings from the private market through issuance of the Bank's own obligations, such as debentures, are considered as borrowings and not receipts, and therefore cannot be accounted for as budget offsets. Thus, the Bank, in order to have the proceeds from such sales credited as budget receipts, has been compelled to use a complicated and costly form of asset sale (certificates of beneficial interest), which is difficult to market because it is non-negotiable and not a familiar instrument to investors. In fact, the low net budget outlays attributable to the Bank in the last 2 fiscal years were realized through this procedure.

<sup>9/</sup> The credit budget used in the fiscal years 1980 and 1981 budgets does not contain a deficit based on net figures. It consists only of gross new commitments to extend credit.

would have to add the two deficits together--a situation similar to that which pertains today. The unified budget deficit alone is not a complete indicator of the government's demands on the credit markets. To it must be added the off-budget deficit and net loans guaranteed. Therefore, explicitly separating direct loans from the unified budget deficit does not create a new deficit that the Congress must worry about; instead, it simply explicates more clearly the elements that the Congress ought to be considering today.

Removing direct lending from the unified budget could either be done as part of legislation establishing the credit budget as part of the Congressional budget process, or it could be accomplished as part of a general restructuring of the budgetary process. In its 1982 budget, the Carter Administration proposed the creation of a budget concepts commission to consider various unresolved issues concerning credit budgeting. In addition to the issue of FFB financing of CBO sales and direct loans to guaranteed borrowers, such a commission could examine the adequacy of credit program administration, uniform rules and procedures for federal credit programs, and the relationship of tax-exempt financing to overall credit and tax policies. The agenda of a budget concepts commission could also be expanded beyond credit issues to consider the structure of the entire budget, including ways to simplify its presentation and improve the nature of the information it provides.

### CONCLUSION

Of these approaches, the last--restructuring the unified and credit budgets--is by far the most comprehensive and ambitious. It could result in a new dual budget system for the allocation of resources. Because credit programs would have no outlay effects, except for defaults and subsidies, the question of how to treat the FFB activities would become nearly moot. This approach would also avoid the outlay impact of changing the unified budget treatment of these activities. In addition, it would enhance the visibility of the credit budget deficit, which now receives little or no attention, as compared to the unified budget deficit.

Of the four alternatives that operate within the framework of the unified budget, the two that focus on the transactions themselves are clearly superior to those that focus only on the FFB. Of these two, changing the budgetary treatment of CBO sales and FFB direct loans to guaranteed borrowers is preferable. The sizable impact on the unified budget deficit of this alternative,

however, might make it unpalatable to any Administration or Congress unless it were phased in, perhaps by implementation in a future fiscal year. Until then, controlling the transactions with the FFB through limitations in the credit budget could be an intermediate step that would assist the Congress and the Administration to come to grips with the resource allocation question without forcing them to absorb the large outlay effects immediately. This option could also be used as an intermediate step if it were decided to establish a budget concepts commission to consider the restructuring of the unified and credit budgets.

